

Internal Revenue Service

Tax Exempt and Government Entities
Exempt Organization
1100 Commerce St
Dallas, TX 75242

Department of the Treasury

UIL: 501.07-01

Release Number: **201343025**

Release Date: 10/25/2013

Date: December 5, 2012

Taxpayer Identification Number:

Form:

Legend:

ORG = Name of Organization

Address = Address of ORG

Tax Year(s) Ended:

Person to Contact/ID Number:

ORG

Address

Contact Numbers:

Phone:

Fax:

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear ,

In a determination letter dated March 29, 1996, you were held to be exempt from Federal income tax under section 501(c)(7) of the Internal Revenue Code (the Code).

Based on recent information received, we have determined you have not operated in accordance with the provisions of section 501(c)(7) of the Code. Accordingly, your exemption from Federal income tax is revoked effective January 1, 20xx. This is a final adverse determination letter with regard to your status under section 501(c)(7) of the Code.

We previously provided you a report of examination explaining why we believe revocation of your exempt status is necessary. At that time, we informed you of your right to contact the Taxpayer Advocate, as well as your appeal rights. On August 21, 20xx, you signed Form 6018-A, Consent to Proposed Action, agreeing to the revocation of your exempt status under section 501(c)(7) of the Code.

You are therefore required to file Form 1120, U.S. Corporate Income Tax Return, for the years ended December 31, 20xx with the Ogden Service Center. For future periods,

you are required to file Form 1120 with the appropriate service center indicated in the instructions for the return.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free, 1-877-777-4778, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

Internal Revenue Service
Office of the Taxpayer Advocate

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter.

Thank you for your cooperation.

Sincerely,

Nanette M. Downing
Director, EO Examinations

Internal Revenue Service
Tax Exempt and Government Entities
Exempt Organization

Department of the Treasury

Date: August 8, 2012

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

ORG = Name of Organization
Address = Address of ORG
Year = xx

Person to Contact/ID Number:

Contact Numbers:
Phone:

Dear ,

We are enclosing a draft copy of our report of examination explaining why we believe the revocation of your organization's exempt status is necessary.

If you accept our findings, please sign and return the enclosed Form 6018-A, Consent to Proposed Action. The Form 6018-A must be signed by officers of the organization. We will then send you a final letter revoking your exempt status.

We request that you respond within 30 days from the date of this letter.

If you do not agree with our position you may appeal your case. You will need to notify the revenue agent named above. A final report and a 30-day letter will be issued to you. The Publication 3498, The Examination Process, explains how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

Following the issuance of the final 30-day letter, you will have 30 days to provide a written statement of appeals telling us why you do not agree with our determination. We will forward your written statement of protest to the Appeals Office and they will contact you. If you and Appeals do not agree on some or all of the issues after your Appeals conference, or if you do not request an Appeals conference, you may file suit in the United States Tax Court, the United States Court of Federal Claims, or the United States District Court, after satisfying procedural and jurisdictional requirements.

You may also request that we refer this matter for technical advice as explained in Publication 892, How to Appeal an IRS Decision on Tax-Exempt Status. If a determination letter is issued to you based on technical advice, no further administrative appeal is available to you within the IRS on the issue that was the subject of the technical advice. Publications 3498 and 892 are available on the Internal Revenue Services website at www.irs.gov.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free, 1-877-777-4778, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

Internal Revenue Service
Office of the Taxpayer Advocate

In the event of revocation, you will be required to file Federal income tax returns for any years after the tax period(s) shown above. File returns with the appropriate service center indicated in the instructions for those returns.

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Enclosure:
Form 6018-A,
Draft Report of Examination

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit 1
Name of Taxpayer ORG		Year/Period Ended 20xx

Legend:

ORG = Name of Organization

Year = xx

ISSUE

Whether the ORG continues to be qualified as a social club under Internal Revenue Code (IRC) § 501(c)(7) due to substantial activities with nonmembers and failing to maintain adequate records.

FACTS

The ORG (Club) was granted exemption from federal income tax under IRC § 501(c)(7), social club, as indicated on their determination letter dated March 29, 19xx. Its application for recognition of exemption, form 1024, states the Club's purpose is to provide a sports oriented, recreational facility for its membership by operating a golf and country club promoting golf, swimming and other sports related activities.

The Club's facilities consist of a Club House containing bars, a restaurant, and event space, an 18 hole golf course, driving range and swimming pool. During 20xx, the restaurant and bars were rented out to a 3rd party. The 20xx form 990 showed a loss of \$ on rents of \$.

The Club's 20xx and 20xx form 990 and 990-T had been previously examined. An advisory had been issued instructing the Club to:

- Correct its signage to indicate the Club was private.
- Follow Revenue Procedure 71-17, 1971-1 C.B. 683 to comply with record-keeping requirements in order to substantiate nonmember usage.
- Maintain documentation as to the reasonableness of exempt and nonexempt expense allocation.
- Monitor nonmember usage of the Club's facilities and services in order to comply with Public Law 94-568 requirement of less than 15% of gross receipts as defined in Rev Proc 71-17.

The Club was advised that a follow-up examination would be conducted to ensure future compliance.

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During the 20xx examination of the Club's form 990 and 990-T, it was determined the Club had not maintained records which followed Rev. Proc. 71-17 in accordance with the previously issued advisory.

The Club had a continued its failure to maintain documentation as to whether members paid for their guest when the group consisted of eight or less individuals, or when groups greater than eight consisted of percent members. In these cases, payment for services is assumed to be made by the members for guests. The Club also did not follow Rev. Proc. 71-17 Sec. 4.01 through 4.09 record keeping requirements. Rev. Proc 71.17, Sec. 4.04 precludes the use of minimum gross receipts standard or audit assumptions as described above in cases where documentation has not been maintained. The Club has not maintained required documentation that it is operating for an exempt purpose.

The Club Manager indicated during the examination's initial interview that guests traditionally paid their fees.

Nonmember income during 20xx was calculated at % as follows:

Account	Account Description	Total	Nonmember
0	Membership Dues	\$ 0	
	Corporate Green Fees		0
0	Green Fees Regular	0	0
0	Green Fees Outings	0	0
0	Green Fees Outings Cart Rental-Member	0	0
0	Cart Rental-Total	0	0
0	Golf Service Fees	0	
0	Pool Guest Fees	0	0
		\$0	\$

Nonmember percentage of gross receipts %

Income from nonmembers included green fees, cart rentals, pool and driving range use.

Signage at the entrance to the Club's facility read "Course Now Open, Public Welcome." The Club's website, , advertises "open to the public" also. The Club House facilities are currently being used for nonmember meetings and events. The restaurant has closed following the bankruptcy filing of its operator,

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No documentation regarding the basis for the expense allocation between exempt and nonexempt purposes was available from the Club.

LAW

Internal Revenue Code (IRC) § 501(c)(7) states "Clubs organized for pleasure, recreation, and other nonprofitable purposes, substantially all of the activities of which are for such purposes and no part of the net earnings of which inures to the benefit of any private shareholder" shall be exempt from taxation.

IRC § 512(a)(3) provides the unrelated business taxable income (UBTI) of organizations described in Internal Revenue Code sections 501(c)(7) includes all gross income, less deductions directly connected with producing that income, but not including exempt function income. Exempt function income is gross income from dues, fees, charges, or similar items paid by members for the purposes for which exempt status was granted to the organization. Exempt function income also includes income that is set aside for qualified purposes.

Treasury Regulation § 1.501(c)(7)-1(b) provides that a club which engages in business, such as makes its social and recreational facilities available to the public is not organized and operated exclusively for pleasure, recreation, and other nonproftable purposes and is not exempt under section 501(a). Solicitation by advertisement or otherwise for public patronage of its facilities is prima fade evidence that an organization is engaging in business and is not being operated exclusively for pleasure, recreation, or social purposes.

Treasury Regulation § 1.512(a)-1 provides that where an organization uses its facilities or personnel for both exempt and non-exempt purposes, expenses must be allocated on a reasonable basis and are to be proximately and primarily related to the activity. An organization is required to maintain appropriate documentation to substantiate the reasonableness of the allocations made.

Revenue Procedure 71-17, 1971-1 C.B. 683 sets forth guidelines for determining the effect of gross receipts derived from nonmember use of a social club's facilities on exemption under Internal Revenue Code Section 501(c)(7) and recordkeeping requirements. Failure to maintain such records or make them available to the Service for examination will preclude use of the minimum gross receipts standard and audit assumptions set forth in this Revenue Procedure. All income derived from the use of your facilities may be considered unrelated business income and subject to income tax.

Section 4.03 requires additional recordkeeping on all occasions other than documented groups of eight or fewer or when 75% of the groups are members. The additional information required includes:

- The date;

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit 1
Name of Taxpayer ORG		Year/Period Ended 20xx

- The total number in the party
- The nonmembers in the party;
- The total charges;
- The charges attributable to nonmembers;
- The charges paid by nonmembers;
- A signed statement by the member as to the amount of reimbursement from nonmembers;
- A signed statement by the member when the member's employer makes payment for nonmembers indicating the name of the employer, the amount paid for the nonmember, the nonmember's name and relationship to the member and purpose served.
- A member signed statement for nonmember gratuitous payment for a member including the amount, donor's name and relationship and the nature of the payment.

Public Law 94-568 provides not more than 15 percent of the gross receipts should be derived from the use of a social club's facilities or services by the general public. An exempt social club may receive up to 35 percent of its gross receipts from a combination of investment income and receipts from non-members, so long as the latter do not represent more than 15 percent of total receipts. Gross receipts are defined for this purpose as those receipts from normal and usual activities traditionally conducted by clubs of the same general type.

TAXPAYER'S POSITION

The Club's Manager states the Club could not be profitable without income from public use at the current membership level and has agreed with the Government.

GOVERNMENT'S POSITION

It was determined during the examination that the Club:

- exceeded the limitation of 15% percentage of gross nonmember income to total gross receipts as set forth by Rev Proc 71-17 and P.L. 94-568,
- failed to comply with the prior examination's advisory instructions relating to public use signage, documentation of nonmember use and method of expense allocation in determining unrelated business income,
- advertised the public use of its facilities,
- failed to document nonmember income.

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The identification and recording of nonmember income is a fundamental tax requirement of a membership organization, whether it is taxable under Section 277 of the Code or tax exempt under Section 501(c)(7) of the Code. Gathering the necessary information regarding nonmember income is often done by coding entries in the accounting system properly and having members sign a form regarding payment of expenses for parties of more than eight. Clubs must recognize the importance of record keeping for nonmember activities and the recording of such activity at the time of a sale. Throughout the examination, it was determined there was inadequate record keeping as well as substantial nonmember activity.

It is the Government's position that the Club is no longer operated exclusively for the pleasure and recreation of its members and is not exempt under IRC Section 501(c)(7).

CONCLUSION

The IRC Section 501(c)(7) tax exempt status of the should be revoked since the nonmember income received by the Club exceeded 15% of the Club's total gross receipts for the year under examination and in prior years.

Further, the Club advertises the use of their facilities to the general public reflecting evidence that it is engaged in a business and is not being "operated exclusively for pleasure, recreation, or social purposes."

As the Club no longer meets the requirements to qualify as exempt from federal income tax under IRC section 501(a) as described in section 501(c)(7), your exempt status under 501(c)(7) of the Internal Revenue Code will be revoked effective January 1, 20xx.

As a taxable entity, the organization is required to file Form 1120, U.S. Corporation Income Tax Return, for all periods following December 31, 20xx.

IRC § 277(a) stipulates in the case of a membership organization which is not exempt from taxation, deductions for the taxable year attributable to furnishing services, goods or other items of value to members shall be allowed only to the extent of income derived from members.